

**UNITED STATES OF AMERICA**  
**Before the**  
**OFFICE OF THRIFT SUPERVISION**

In the Matter of	)	
	)	Order No.: CN 11-11
	)	
<b>LAKE CITY FEDERAL BANK</b>	)	Effective Date: May 12, 2011
	)	
Lake City, Minnesota	)	
OTS Docket No. 02828	)	
	)	

**ORDER TO CEASE AND DESIST**

**WHEREAS**, Lake City Federal Bank, Lake City, Minnesota, OTS Docket No. 02828 (Association), by and through its Board of Directors (Board), has executed a Stipulation and Consent to Issuance of an Order to Cease and Desist (Stipulation); and

**WHEREAS**, the Association, by executing the Stipulation, has consented and agreed to the issuance of this Order to Cease and Desist (Order) by the Office of Thrift Supervision (OTS) pursuant to 12 U.S.C. § 1818(b); and

**WHEREAS**, pursuant to delegated authority, the OTS Regional Director for the Central Region (Regional Director) is authorized to issue Orders to Cease and Desist where a savings association has consented to the issuance of an order.

**NOW, THEREFORE, IT IS ORDERED that:**

**Cease and Desist.**

1. The Association and its directors, officers, and employees shall cease and desist from any action (alone or with others) for or toward, causing, bringing about, participating in, counseling,

or aiding and abetting the unsafe or unsound practices and/or violations of law or regulation that resulted in the Association operating with: (a) an excessive level of adversely classified loans; and (b) inadequate earnings to augment capital as described in the comprehensive OTS Report of Examination of the Association dated December 6, 2010 (2010 ROE).

**Capital.**

2. By June 30, 2011, the Association shall have and maintain: a Tier 1 (Core) Capital Ratio equal to or greater than eight and one-half percent (8.5%) after the funding of an adequate Allowance for Loan and Lease Losses (ALLL) and a Total Risk-Based Capital Ratio equal to or greater than twelve percent (12%).<sup>1</sup>

3. By September 30, 2011, the Association shall have and maintain a Tier 1 (Core) Capital Ratio equal to or greater than nine percent (9%) after the funding of an adequate Allowance for Loan and Lease Losses (ALLL) and a Total Risk-Based Capital Ratio equal to or greater than twelve percent (12%).

**Capital and Business Plan.**

4. By June 30, 2011, the Association shall submit to the Regional Director a written plan (Capital and Business Plan) for the period beginning with July 1, 2011 through December 31, 2013 addressing the requirements of this Order and including capital enhancement strategies necessary for the Association to have and maintain capital at the levels prescribed in Paragraphs 2 and 3. At a minimum, the Capital and Business Plan shall:

- (a) identify the specific sources and methods by which additional capital will be raised to achieve and maintain the Association's capital at the level prescribed in

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<sup>1</sup> The requirement in Paragraphs 2 and 3 to have and maintain a specific capital level means that the Association may not be deemed to be "well-capitalized" for purposes of 12 U.S.C. §1831o and 12 C.F.R. Part 565, pursuant to 12 C.F.R. §565.4(b)(1)(iv).

Paragraphs 2 and 3;

- (b) detail the Association's capital preservation and enhancement strategies with specific narrative goals;
- (c) contain operating strategies to achieve realistic core earnings;
- (d) include quarterly financial projections (balance sheet and income statement), including Tier 1 (Core) and Total Risk Based Capital Ratios, for the period covered by the Capital and Business Plan; and
- (e) identify all relevant assumptions made in formulating the Capital and Business Plan and include a requirement that documentation supporting such assumptions be retained by the Association.

5. Upon receipt of written notice of non-objection from the Regional Director to the Capital and Business Plan, the Association shall implement and adhere to the Capital and Business Plan. A copy of the Capital and Business Plan shall be provided to the Regional Director within seven (7) days after Board approval.

6. Any material modifications<sup>2</sup> to the Capital and Business Plan must receive the prior written non-objection of the Regional Director. The Association shall submit proposed material modifications to the Regional Director at least forty-five (45) days prior to implementation.

7. By September 30, 2012, and each September 30th thereafter, the Capital and Business Plan shall be updated and submitted to the Regional Director pursuant to Paragraph 4 above and shall incorporate the Association's budget plan and profit projections for the next two (2) fiscal years taking into account any revisions to the Association's loan, investment and operating

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<sup>2</sup> A modification shall be considered material under this Paragraph if the Association (a) plans to engage in any activity that is inconsistent with the Capital and Business Plan; or (b) exceeds the level of any activity contemplated in the Capital and Business Plan by more than ten percent (10%).

policies.

**Capital and Business Plan Variance Reports.**

8. Within forty-five (45) days after the end of each quarter, after implementation of the Capital and Business Plan, the Board shall review written quarterly variance reports on the Association's compliance with its Capital and Business Plan (Variance Reports). The Board's review of Variance Reports and compliance with the Capital and Business Plan shall include a review of the internal and external risks affecting the Association's ability to successfully implement the Capital and Business Plan. The minutes of the Board meeting shall fully document the Board's review and discussion. The Variance Reports shall:

- (a) identify variances in the Association's actual performance during the preceding quarter as compared to the projections set forth in the Capital and Business Plan;
- (b) contain an analysis and explanation of identified variances; and
- (c) discuss the specific measures taken or to be taken by the Association to address identified variances.

9. A copy of each Variance Report shall be provided to the Regional Director within seven (7) days after the Board meeting at which it was reviewed and discussed.

**Contingency Plan.**

10. Within fifteen (15) days after: (a) the Association fails to meet the capital requirements prescribed in Paragraphs 2 or 3; (b) the Association fails to comply with the Capital and Business Plan prescribed in Paragraph 4; or (c) any written request from the Regional Director, the Association shall submit a written Contingency Plan that is acceptable to the Regional Director.

11. The Contingency Plan shall detail the actions to be taken, with specific time frames, to achieve one of the following results by the later of the date of receipt of all required regulatory

approvals or sixty (60) days after the implementation of the Contingency Plan: (a) merger with, or acquisition by, another federally insured depository institution or holding company thereof; or (b) voluntary dissolution by filing an appropriate application with the OTS in conformity with applicable laws, regulations and regulatory guidance.

12. Upon receipt of written notification from the Regional Director, the Association shall implement and adhere to the Contingency Plan immediately. The Association shall provide the Regional Director with written status reports detailing the Association's progress in implementing the Contingency Plan by no later than the first (1<sup>st</sup>) and fifteenth (15<sup>th</sup>) of each month following implementation of the Contingency Plan.

**Asset Quality.**

13. By July 30, 2011, the Association shall develop individual written specific workout plans for each adversely classified asset or group of such classified assets to any one borrower or loan relationship of five hundred thousand dollars (\$500,000) or greater, including unfunded loan commitments (collectively, Asset Workout Plans).

14. Within forty-five (45) days after the end of each quarter, beginning with the quarter ending September 30, 2011, the Association shall submit a quarterly written asset status report (Quarterly Asset Report) to the Board. The Board's review of the Quarterly Asset Report shall be documented in the Board meeting minutes. The Quarterly Asset Report shall include, at a minimum:

- (a) the current status of all Asset Workout Plans;
- (b) the ratio of all classified assets to Tier 1 (Core) capital plus ALLL;
- (c) a comparison of all classified assets at the current quarter end with the preceding quarter;

(d) a discussion of the actions taken during the preceding quarter to reduce the Association's level of classified assets; and

(e) any recommended revisions or updates to the Asset Workout Plans.

15. Within sixty (60) days after the end of each quarter, beginning with the quarter ending September 30, 2011, a copy of the Quarterly Asset Report shall be provided to the Regional Director.

**Regulatory Financial Reporting Policy.**

16. Within forty-five (45) days, the Association shall develop and implement written policies and procedures to ensure that the Association's regulatory financial reports filed with the OTS are timely and accurately prepared in compliance with all applicable laws, regulations, and regulatory guidance and to address all corrective actions set forth in the 2010 ROE relating to regulatory reporting (Regulatory Financial Reporting Policy). The Regulatory Financial Reporting Policy shall address procedures for amending inaccurate regulatory financial filings. The Board's review of the Regulatory Financial Reporting Policy shall be documented in the Board minutes and a copy of the Regulatory Financial Reporting Policy shall be submitted to the Regional Director within seven (7) days after the Board meeting at which such it was reviewed and adopted.

**Independent Review of Appraisals.**

17. Within forty-five (45) days, the Association shall implement an independent review and analysis process to ensure that appraisals conform to all applicable laws, regulations, and regulatory guidance, including appraisal standards. The appraisal review and analysis process shall ensure that:

(a) appraisals are performed in accordance with 12 C.F.R. Part 564; and

- (b) appraisals are consistent with the guidance set forth in OTS CEO Memo 371, "Final Interagency Appraisal and Evaluation Guidelines" (December 2, 2010); and
- (c) written documentation supporting each appraisal review and analysis is retained in the loan file along with the appraisal.

**Allowance for Loan and Lease Losses.**

18. Within thirty (30) days after the end of each quarter, beginning with the quarter ending June 30, 2011, the Association shall analyze the adequacy of the ALLL consistent with its ALLL Policy (Quarterly ALLL Report). The Board's review of the Quarterly ALLL Report, including, the Association's documentation supporting the calculation, shall be fully documented in the Board meeting minutes. Any deficiency in the ALLL shall be remedied by the Association in the quarter in which it is discovered and before the Association files its TFR with the OTS. A copy of the Quarterly ALLL Report and the Board meeting minutes detailing the Board's review shall be provided to the Regional Director within fifteen (15) days after the Board meeting.

**Violations of Law.**

19. Within thirty (30) days, the Association shall ensure that all violations of law and/or regulation discussed in the 2010 ROE are corrected and that adequate policies, procedures and systems are established or revised and thereafter implemented to prevent future violations.

**Management and Directorate Oversight.**

20. Within forty-five (45) days, the Association shall retain an independent third-party acceptable to the Regional Director to conduct a management review (Management Study).

21. Within ninety (90) days, a copy of the Management Study shall be forwarded simultaneously to the Board and to the Regional Director.

22. Within one hundred twenty (120) days, the Board shall submit to the Regional Director a

written plan to address any identified weaknesses or deficiencies noted in the Management Study (Management Plan).

**Growth.**

23. Effective immediately, the Association shall not increase its total assets during any quarter in excess of an amount equal to net interest credited on deposit liabilities during the prior quarter without the prior written non-objection of the Regional Director.

**Golden Parachute Payments.**

24. Effective immediately, the Association shall not make any golden parachute payment<sup>3</sup> unless, with respect to such payment, the Association has complied with the requirements of 12 C.F.R. Part 359.

**Directorate and Management Changes.**

25. Effective immediately, the Association shall comply with the prior notification requirements for changes in directors and Senior Executive Officers set forth in 12 C.F.R. Part 563, Subpart H.

**Employment Contracts and Compensation Arrangements.**

26. Effective immediately, the Association shall not enter into any new contractual arrangement or renew, extend, or revise any contractual arrangement relating to compensation or benefits for any director or Senior Executive Officer of the Association, unless it first provides the Regional Director with not less than thirty (30) days prior written notice of the proposed transaction. The notice to the Regional Director shall include a copy of the proposed employment contract or compensation arrangement or a detailed, written description of the compensation arrangement to be offered to such director or Senior Executive Officer, including

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<sup>3</sup> The term “golden parachute payment” is defined at 12 C.F.R. § 359.1(f).



all benefits and perquisites. The Board shall ensure that any contract, agreement, or arrangement submitted to the Regional Director fully complies with the requirements of 12 C.F.R. Part 359, 12 C.F.R. §§ 563.39 and 563.161(b), and 12 C.F.R. Part 570 – Appendix A.

**Third Party Contracts.**

27. Effective immediately, the Association shall not enter into any arrangement or contract with a third party service provider that is significant to the overall operation or financial condition of the Association<sup>4</sup> or outside the Association's normal course of business unless, with respect to each such contract, the Association has: (a) provided the Regional Director with a minimum of thirty (30) days prior written notice of such arrangement or contract and a written determination that that the arrangement or contract complies with the standards and guidelines set forth in OTS Thrift Bulletin 82a; and (b) received written notice of non-objection from the Regional Director.

**Brokered Deposits.**

28. Effective immediately, the Association shall comply with the requirements of 12 C.F.R. § 337.6(b). The Association shall provide to the Regional Director a copy of any waiver request submitted to the Federal Deposit Insurance Corporation.

**Effective Date, Incorporation of Stipulation.**

29. This Order is effective on the Effective Date as shown on the first page. The Stipulation is made a part hereof and is incorporated herein by this reference.

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<sup>4</sup> A contract will be considered significant to the overall operation or financial condition of the Association where the annual contract amount equals or exceeds two percent (2%) of the Association's total capital, where there is a foreign service provider, or where it involves information technology that is critical to the Association's daily operations without regard to the contract amount.

**Duration.**

30. This Order shall remain in effect until terminated, modified, or suspended, by written notice of such action by the OTS, acting by and through its authorized representatives.

**Time Calculations.**

31. Calculation of time limitations for compliance with the terms of this Order run from the Effective Date and shall be based on calendar days, unless otherwise noted.

32. The Regional Director or an OTS authorized representative may extend any of the deadlines set forth in the provisions of this Order upon written request by the Association that includes reasons in support for any such extension. Any OTS extension shall be made in writing.

**Submissions and Notices.**

33. All submissions, including any reports, to the OTS that are required by or contemplated by this Order shall be submitted within the specified timeframes.

34. Except as otherwise provided herein, all submissions, requests, communications, consents, or other documents relating to this Order shall be in writing and sent by first class U.S. mail (or by reputable overnight carrier, electronic facsimile transmission, or hand delivery by messenger) addressed as follows:

(a) **To the OTS:**

Regional Director  
Office of Thrift Supervision  
One South Wacker Drive, Suite 2000  
Chicago, Illinois 60606  
Facsimile: (312) 917-5001

(b) **To the Association:**

Chairman of the Board  
Lake City Federal Bank  
201 East Marion Street  
Lake City, Minnesota 55041  
Facsimile: (651) 345-5539

35. Following the Transfer Date,<sup>5</sup> all submissions, requests, communications, consents or other documents relating to this Order shall be directed to the Comptroller of the Currency, or to the individual, division, or office designated by the Comptroller of the Currency.

**No Violations Authorized.**

36. Nothing in this Order or the Stipulation shall be construed as allowing the Association, its Board, officers, or employees to violate any law, rule, or regulation.

**IT IS SO ORDERED.**

**OFFICE OF THRIFT SUPERVISION**

By: \_\_\_\_\_/s/  
Daniel T. McKee  
Regional Director, Central Region

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<sup>5</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. Law No. 111-203, § 311, 124 Stat. 1520 – 21 (2010).

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In the Matter of	)	
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<b>LAKE CITY FEDERAL BANK</b>	)	Effective Date: May 12, 2011
	)	
	)	
Lake City, Minnesota	)	
OTS Docket No. 02828	)	
	)	

**STIPULATION AND CONSENT TO ISSUANCE OF ORDER TO CEASE AND DESIST**

**WHEREAS**, the Office of Thrift Supervision (OTS), acting by and through its Regional Director for the Central Region (Regional Director), and based upon information derived from the exercise of its regulatory and supervisory responsibilities, has informed Lake City Federal Bank, Lake City, Minnesota, OTS Docket No. 02828 (Association) that the OTS is of the opinion that grounds exist to initiate an administrative proceeding against the Association pursuant to 12 U.S.C. § 1818(b);

**WHEREAS**, the Regional Director, pursuant to delegated authority, is authorized to issue Orders to Cease and Desist where a savings association has consented to the issuance of an order; and

**WHEREAS**, the Association desires to cooperate with the OTS to avoid the time and expense of such administrative cease and desist proceeding by entering into this Stipulation and Consent to the Issuance of Order to Cease and Desist (Stipulation) and, without admitting or

denying that such grounds exist, but only admitting the statements and conclusions in Paragraphs 1 and 2 below concerning Jurisdiction, hereby stipulates and agrees to the following terms:

**Jurisdiction.**

1. The Association is a “savings association” within the meaning of 12 U.S.C. § 1813(b) and 12 U.S.C. § 1462(4). Accordingly, the Association is an “insured depository institution” as that term is defined in 12 U.S.C. § 1813(c).
2. Pursuant to 12 U.S.C. § 1813(q), the Director of the OTS is the “appropriate Federal banking agency” with jurisdiction to maintain an administrative enforcement proceeding against a savings association. Therefore, the Association is subject to the authority of the OTS to initiate and maintain an administrative cease and desist proceeding against it pursuant to 12 U.S.C. § 1818(b).

**OTS Findings of Fact.**

3. Based on a comprehensive examination of the Association dated December 6, 2010 (2010 ROE), the OTS finds that the Association has engaged in unsafe or unsound banking practices and/or violations of law or regulation that resulted in the Association operating with:  
(a) an excessive level of adversely classified loans; and (b) inadequate earnings to augment capital as described in the 2010 ROE.

**Consent.**

4. The Association consents to the issuance by the OTS of the accompanying Order to Cease and Desist (Order). The Association further agrees to comply with the terms of the Order upon the Effective Date of the Order and stipulates that the Order complies with all requirements of law.

**Finality.**

5. The Order is issued by the OTS under 12 U.S.C. § 1818(b). Upon the Effective Date, the Order shall be a final order, effective, and fully enforceable by the OTS under the provisions of 12 U.S.C. § 1818(i).

**Waivers.**

6. The Association waives the following:

- (a) the right to be served with a written notice of the OTS's charges against it as provided by 12 U.S.C. § 1818(b) and 12 C.F.R. Part 509;
- (b) the right to an administrative hearing of the OTS's charges as provided by 12 U.S.C. § 1818(b) and 12 C.F.R. Part 509;
- (c) the right to seek judicial review of the Order, including, without limitation, any such right provided by 12 U.S.C. § 1818(h), or otherwise to challenge the validity of the Order; and
- (d) any and all claims against the OTS, including its employees and agents, and any other governmental entity for the award of fees, costs, or expenses related to this OTS enforcement matter and/or the Order, whether arising under common law, federal statutes or otherwise.

**OTS Authority Not Affected.**

7. Nothing in this Stipulation or accompanying Order shall inhibit, estop, bar, or otherwise prevent the OTS from taking any other action affecting the Association if at any time the OTS deems it appropriate to do so to fulfill the responsibilities placed upon the OTS by law.

**Other Governmental Actions Not Affected.**

8. The Association acknowledges and agrees that its consent to the issuance of the Order is solely for the purpose of resolving the matters addressed herein, consistent with Paragraph 7 above, and does not otherwise release, discharge, compromise, settle, dismiss, resolve, or in any way affect any actions, charges against, or liability of the Association that arise pursuant to this action or otherwise, and that may be or have been brought by any governmental entity other than the OTS.

**Miscellaneous.**

9. The laws of the United States of America shall govern the construction and validity of this Stipulation and of the Order.

10. If any provision of this Stipulation and/or the Order is ruled to be invalid, illegal, or unenforceable by the decision of any Court of competent jurisdiction, the validity, legality, and enforceability of the remaining provisions hereof shall not in any way be affected or impaired thereby, unless the Regional Director in his or her sole discretion determines otherwise.

11. All references to the OTS in this Stipulation and the Order shall also mean any of the OTS's predecessors, successors, and assigns.

12. The section and paragraph headings in this Stipulation and the Order are for convenience only and shall not affect the interpretation of this Stipulation or the Order.

13. The terms of this Stipulation and of the Order represent the final agreement of the parties with respect to the subject matters thereof, and constitute the sole agreement of the parties with respect to such subject matters.

14. The Stipulation and Order shall remain in effect until terminated, modified, or suspended in writing by the OTS, acting through its Regional Director or other authorized representative.

**Signature of Directors/Board Resolution.**

15. Each Director signing this Stipulation attests that he or she voted in favor of a Board Resolution authorizing the consent of the Association to the issuance of the Order and the execution of the Stipulation. This Stipulation may be executed in counterparts by the directors after approval of execution of the Stipulation at a duly called board meeting.

**WHEREFORE**, the Association, by its directors, executes this Stipulation.

**LAKE CITY FEDERAL BANK**  
**Lake City, Minnesota**

Accepted by:  
**Office of Thrift Supervision**

\_\_\_\_\_/s/\_\_\_\_\_  
Charles P. Wise, Chairman

By:\_\_\_\_\_/s/\_\_\_\_\_  
Daniel T. McKee  
Regional Director, Central Region

\_\_\_\_\_/s/\_\_\_\_\_  
Randall L. Ahrens, Director

Date: See Effective Date on page 1

\_\_\_\_\_/s/\_\_\_\_\_  
Kathleen A. Durand, Director

\_\_\_\_\_/s/\_\_\_\_\_  
Glenn J. Dwelle, Sr., Director

\_\_\_\_\_/s/\_\_\_\_\_  
Philip A. Gartner, Director

\_\_\_\_\_/s/\_\_\_\_\_  
Mark A. Prenger, Director